FDIC State Profile

WINTER 2003

Kentucky

Weak economic and industrial conditions in Kentucky are reflected by labor market data.

- The state unemployment rate of 5.9 percent in third quarter 2003 was up from 5.5 percent a year earlier.
- After improving in late 2002 and early 2003, the pace of job loss in Kentucky intensified, leaving third-quarter payroll employment 0.9 percent below the previous year.
- The most significant job losses were in Kentucky's largest sectors: manufacturing; trade, transportation, utilities; and government (see Chart 1). With the exception of positive hiring in education and health services, Kentucky's other sectors (construction; financial; leisure and hospitality; professional and business services; and information services) experienced smaller declines.
- The past year's employment gains in the ***Owensboro*** MSA reflect modest hiring by education and healthcare providers, local government, and several other sectors. Owensboro Mercy Health System and River Valley Behavioral Health are two of the top employers in the MSA.
- In the ***Evansville-Henderson*** MSA, the largest job losses in the past year were in the transportation and trade sector, manufacturing, construction, and public education (see Chart 2).

Weak labor markets affected household finances.

- Continued employment losses contributed to a 14 percent year-over-year increase in third-quarter personal bankruptcy filings, noticeably higher than the 9.5 percent increase recorded in third quarter 2002.
- Real personal income growth in Kentucky slowed to 1.4 percent in second quarter 2003 from 2.4 percent a year earlier.[1] Yet Kentucky and Wisconsin stood out among states in the Chicago Region,[2] reporting income growth that was 0.3 to 2.1 percentage points higher than elsewhere.

Kentucky's housing market remained active.

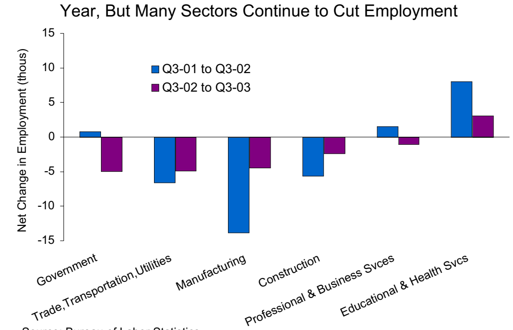
- The housing market in Kentucky continued to show strong activity with home resales posting a record high in third quarter, perhaps spurred temporarily by a desire to buy a home before mortgage rates rose further (see Chart 3).
- Kentucky's housing market activity may slow since demand for new homes has not kept pace with supply in major MSAs.[3]

[1] Real personal income is personal income adjusted for the impact of inflation.

[2] Chicago Region includes Kentucky, Indiana, Illinois, Michigan, Ohio, and Wisconsin.

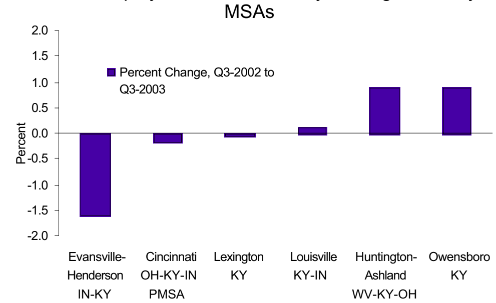
[3] Economy.com, Inc.: *Kentucky Précis,* July 2003.

Chart 1: The Government Sector Lost the Most Jobs in the Past Year, But Many Sectors Continue to Cut Employment



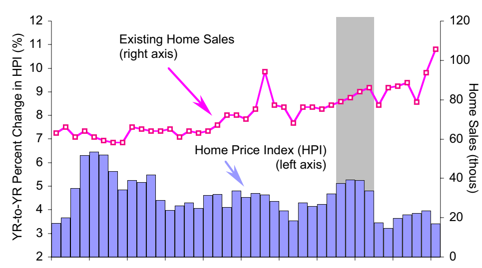
Source: Bureau of Labor Statistics

Chart 2: Employment Patterns Vary Among Kentucky MSAs



Source: Bureau of Labor Statistics

Chart 3: Existing Homes Sales in Kentucky Climb as Home Price Appreciation Slows



Sources: National Association of Realtors; Office of Federal Housing Enterprise Oversight

Home price appreciation rates are low, and continued slow growth in demand may limit future appreciation.

Kentucky banks experienced a moderate decrease in profitability at mid-year.

- Return on assets (ROA), a measure of profitability among community institutions, declined to 0.94 percent in the three months ending June 2003, the lowest aggregate level seen since December 2001.[4]
- The falloff in profitability stemmed from a continued decrease in interest margins driven by a faster decline in yield on earning assets than a decrease in the cost of funds. Net interest income fell to 3.57 percent of average assets, 25 basis points lower than a year ago (see Table 1).
- Noninterest sources of income such as service charges on deposits and other noninterest income saw modest increases in the past year, but these gains were not sufficient to maintain ROA at prior year levels.
- Lower provisions as of June 2003 helped bolster returns for community banks. From June 2002 to June 2003, total loans at community banks declined 4.7 percent while the allowance for loan and lease losses (ALLL) to noncurrent loans remained steady at 118.5 percent. During this same period, net charge-offs to total loans declined 10 basis points.
- Kentucky's community banks did not benefit from the volume of realized gains on securities that banks in other states recognized . As of June 30, 2003, securities gains for Kentucky institutions only totaled 0.06 percent of average assets, compared with 0.26 percent for all banks in the Chicago Region.

Shares of commercial real estate (CRE) loans continued to rise among Kentucky's community institutions.

- Although CRE loan growth has tapered off in the past year, loans backed by commercial real estate have been the only loan category to show continual growth over last decade (see Chart 4).
- CRE-backed loans traditionally yield higher returns, which indicates that increased portfolio shares of CRE have the potential to contribute to net earnings for Kentucky's institutions.
- Yet the potential for loss among CRE loans is traditionally higher than other loan categories.

Delinquency rates are modestly high and rising.

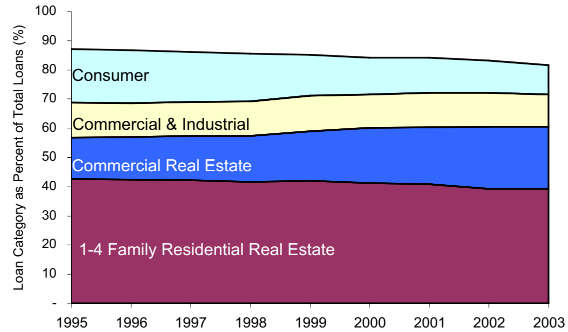
- Although aggregate delinquency rates did not see much movement during the first half of 2003, the past-due and nonaccrual rate (PDNA) in Kentucky banks, 2.7 percent for second quarter 2003, remained slightly higher than rates experienced across the Chicago region.
- All major loan categories, except construction loans, saw an increase in delinquency. The highest PDNA increases were among commercial and industrial loans and consumer loans, which were already the two categories where delinquency levels were the highest (see Chart 5).

Table 1: Impact on Net Income from Lower Net Interest Income Not Offset By Gains Elsewhere

Income statement contribution (as percentage of average assets)	3 months ended June 30		Basis Point Change
	2002	2003	
Net Interest Income	3.82	3.57	-0.25
Total Noninterest Income	0.84	0.93	0.09
Noninterest Expense	-2.85	-2.87	-0.02
Provision Expense	-0.54	-0.49	0.05
Security Gains & Losses	0.05	0.06	0.01
Income Taxes	-0.30	-0.26	0.04
Net Income (ROA)	1.03	0.94	-0.09

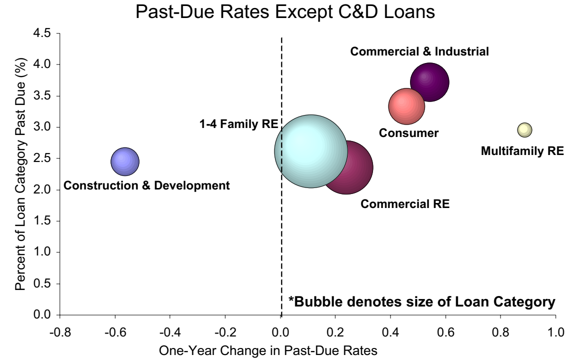
Source: Bank and Thrift Call Reports, aggregate data for community institutions

Chart 4: Commercial Real Estate Is the Only Major Loan Category Showing Growth at Kentucky Institutions



Source: Bank and Thrift Call Reports; aggregate data for six months ending June each year

Chart 5: All Loan Types Experienced an Increase in Past-Due Rates Except C&D Loans



Source: Aggregate Data from Bank and Thrift Call Reports.

[4] Community institutions are non-specialty banks and thrifts more than three years old with assets of $1 billion or less.

Kentucky at a Glance

General Information	Jun-03	Jun-02	Jun-01	Jun-00	Jun-99
Institutions (#)	246	254	263	284	292
Total Assets (in thousands)	50,933,945	57,792,507	56,946,444	54,135,509	55,490,817
New Institutions (# < 3 years)	10	12	16	19	20
New Institutions (# < 9 years)	41	41	41	39	40

Capital	Jun-03	Jun-02	Jun-01	Jun-00	Jun-99
Tier 1 Leverage (median)	9.16	9.22	9.49	9.66	9.36

Asset Quality	Jun-03	Jun-02	Jun-01	Jun-00	Jun-99
Past-Due and Nonaccrual (median %)	2.33%	2.30%	2.33%	1.77%	1.89%
Past-Due and Nonaccrual >= 5%	34	36	38	22	19
ALLL/Total Loans (median %)	1.28%	1.26%	1.17%	1.18%	1.19%
ALLL/Noncurrent Loans (median multiple)	1.42	1.53	1.42	1.68	1.73
Net Loan Losses/Loans (aggregate)	0.49%	0.52%	0.36%	0.22%	0.37%

Earnings	Jun-03	Jun-02	Jun-01	Jun-00	Jun-99
Unprofitable Institutions (#)	13	22	19	18	21
Percent Unprofitable	5.3%	8.7%	7.2%	6.3%	7.2%
Return on Assets (median %)	1.12	1.12	1.03	1.21	1.19
25th Percentile	0.71	0.65	0.64	0.84	0.86
Net Interest Margin (median %)	3.89%	4.03%	3.97%	4.28%	4.14%
Yield on Earning Assets (median)	6.11%	6.91%	8.27%	8.29%	7.88%
Cost of Funding Earning Assets (median)	2.22%	2.92%	4.32%	4.04%	3.77%
Provisions to Avg. Assets (median)	0.19%	0.17%	0.16%	0.15%	0.13%
Noninterest Income to Avg. Assets (median)	0.72%	0.64%	0.64%	0.60%	0.59%
Overhead to Avg. Assets (median)	2.86%	2.80%	2.87%	2.78%	2.78%

Liquidity/Sensitivity	Jun-03	Jun-02	Jun-01	Jun-00	Jun-99
Loans to Deposits (median %)	79.79%	81.55%	83.68%	86.02%	81.46%
Loans to Assets (median %)	65.79%	66.49%	67.34%	68.79%	65.88%
Brokered Deposits (# of institutions)	39	34	41	43	43
Bro. Deps./Assets (median for above inst.)	1.77%	1.19%	0.82%	1.02%	1.71%
Noncore Funding to Assets (median)	19.67%	19.73%	20.80%	19.20%	17.78%
Core Funding to Assets (median)	68.29%	68.86%	67.76%	68.35%	71.00%

Bank Class	Jun-03	Jun-02	Jun-01	Jun-00	Jun-99
State Nonmember	162	165	168	183	186
National	49	51	52	58	61
State Member	9	11	11	9	8
S&L	10	10	10	11	11
Savings Bank	16	17	22	23	26
Mutually Insured	0	0	0	0	0

MSA Distribution	# of Inst.	Assets	% Inst.	% Assets
No MSA	175	23,130,346	71.1%	45.4%
Lexington KY	24	4,505,729	9.8%	8.8%
Louisville KY-IN	16	17,144,235	6.5%	33.7%
Cincinnati OH-KY-IN PMSA	15	3,214,866	6.1%	6.3%
Huntington-Ashland WV-KY-OH	8	1,363,358	3.3%	2.7%
Owensboro KY	3	592,149	1.2%	1.2%
Clarksville-Hopkinsville TN-KY	3	785,878	1.2%	1.5%
Evansville-Henderson IN-KY	2	197,384	0.8%	0.4%